PUTTING INVESTORS FIRST

The Role of State Securities Regulators

NASAA

STATES: *At the Vanguard of Investor Protection*

States are an indispensable early warning system to alert the public, other regulators, and policy makers to problems. State regulators then work with national regulators on market-wide solutions when necessary. State securities regulators investigate and bring enforcement actions - they do not engage in rulemaking for the national markets. That responsibility belongs to the SEC and the SROs. Below are examples where states uncovered a widespread problem and worked with fellow regulators and/or Congress on a national solution.

PROBLEM	ISSUES IDENTIFIED BY STATE SECURITIES REGULATORS	NATIONAL RESPONSE
$2 billion/yr Losses in Penny Stocks	**1989:** States determined penny stock offerings by newly formed shell companies to be fraudulent. These "blank check" companies had no business plan except a future merger with an unidentified company.	**1990:** Congress passed Penny Stock Reform Act, which mandated SEC to adopt special rules governing sale of penny stocks (less than $5 per share) and public offerings of shares in blank check companies (SEC Rule 419).
$6 billion/yr Losses in Micro-cap Stocks	**1996-97:** 33 States participated in a sweep of 15 broker-dealer firms that specialized in aggressively retailing low-priced securities to individual investors. States found massive fraud in firms' manipulation of shares of start-up companies, most of which had no operating history.	**1997-98:** Congress held hearings on fraud in the micro-cap securities markets (shares selling between $5-$10). **2002:** Congress passed the Sarbanes-Oxley Act, which made certain state actions a basis for federal statutory disqualification from the securities industry.
Risks of Securities Offerings on the Internet	**1996-97:** States issued uniform interpretative guidance on use of Internet for legitimate securities offerings and dissemination of product information by licensed financial services professionals.	**1998:** SEC issued interpretative guidance based on the States' model on the use of Internet for securities offerings and dissemination of services and product information by licensed financial services professionals.
Risks of Online Trading	**1999:** In a report on trading of securities on the Internet, States found that investors did not appreciate certain risks, including buying on margin and submitting market orders.	**2001:** SEC approved a new NASD rule requiring brokers to provide individual investors with a written disclosure statement on the risks of buying securities on margin.
Risks of Day Trading	**1999:** In a report on individuals engaged in day trading, States found that day trading firms failed to tell prospective investors that 70% of day traders would lose their investment while the firm earned large trading commissions.	**2000:** SEC approved new NASD rules making day trading firms give written risk disclosure to individual investors. **2001:** SEC approved new NASD and NYSE rules governing margins extended to day traders.
Research Analyst Conflict of Interest	**2002-3:** States investigated and helped focus attention on conflicts of interest between research analyst and major Wall Street firms.	**2002-3:** The SEC, NASD, NYSE, and States reached a landmark $1.4 billion global settlement and firms agree to reform practices.

For More Information:
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HOW STATE SECURITIES REGULATORS SERVE AND PROTECT INVESTORS

States have protected Main Street investors from fraud for nearly 100 years. Securities markets are global but securities are sold locally by professionals who are licensed in every state where they conduct business.

Our nation's unique complementary system of state, federal, and industry regulation ensures fair markets for all investors. Eighty-five million investors rely on regulators to keep our nation's markets well policed and cannot afford any weakening of this successful and complementary regulatory system.

State securities regulators work within your state government to protect investors and help maintain the integrity of the securities industry by:

- **Licensin**g stockbrokers, investment adviser firms (those managing less than $25 million in assets), and securities firms that conduct business in the state.
- **Registering** certain securities offered to the states' investors.
- **Investigating** investor complaints and potential cases of investment fraud.
- **Enforcing** state securities laws by fining, penalizing, providing restitution to investors, prosecuting white-collar criminals, and imposing legally binding conduct remedies designed to correct specific problems.
- **Examining** brokerage and investment adviser firms to ensure compliance with securities laws and maintenance of accurate records of client accounts.
- **Reviewing** certain offerings that are not exempt from state law.
- **Educating** investors about their rights and providing the tools and knowledge they need to make informed financial decisions.
- **Advocating** passage of strong, sensible, and consistent state securities laws and regulations.

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